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Analysis of Business Trends Plus Selected Financial Indicators

Another Curve Ball

As if the economy wasn't having enough trouble eking out admittedly modest gains, another curve ball was recently thrown at the optimists who anticipate a quickening pace of business later this year. This time it was neither an unexpectedly weak economic statistic nor even one "made in America", but came from the economic epicenter of Europe in the form of a hike in Germany's discount rate to a postwar high of 8¾ percent. By prolonging Europe's monetary squeeze, this widely anticipated move heightened the worries of the global investment community that the industrial world was being consigned to an extended period of economic stagnation. And, for good reason. Most of Europe is already mired in the economic doldrums due to the punishing burden of lofty interest rates, Japan is experiencing a sharp business slowdown and, in light of deteriorating business conditions elsewhere, it might only be a matter of time before the muscle of US export growth, which has often provided the razor-thin margin between slow and no growth, turns to flab.

Nonetheless, while the financial and equity markets worldwide were reacting negatively to the German rate hike, they should have been breathing a sigh of relief. For although the Bundesbank possessed several compelling reasons to initiate an outright tightening of monetary policy, ranging from rapid money supply growth to an uncomfortably high rate of consumer price inflation to excessive credit demands, and has often been accused of being insensitive to the pan-European reverberations of its actions, this time around the German central bank tempered its inflation-fighting zeal with a healthy dose of business cycle reality. For when faced with the choice of hiking either the ceiling or the floor of German short-term interest rates, it chose to lift the floor and keep the ceiling; since money market rates hovered much closer to the effective ceiling imposed by the Lombard rate and far from the floor set by the discount rate, the net interest rate effect of the recent Bundesbank initiative was more apparent than real. This was just as well, for lifting the Lombard rate could have set into motion either a pan-European interest rate increase or, if other European Community (EC) members resisted, a severe bout of intra-European currency turbulence which would have jolted the Exchange Rate Mechanism of the European Monetary System.

While policymakers throughout Europe express a modicum of sympathy with Germany's efforts to combat inflation, it is leavened with a large dose of queasiness as to where this all leads. Judging by the latest economic readings, it's leading to economic stagnation and neither Germany, nor much of the rest of Europe, can relish the thought of a further escalation of interest rates. Although pockets of relatively robust business activity do exist, especially in Spain and Portugal, these are the exceptions rather than the rule. In Germany itself, a first quarter snapback in gross national product growth—following two straight quarterly declines—appears to have been short-lived. Renewed evidence of business weakness was in bountiful supply in the second quarter: Real retail sales are tumbling, industrial output is sputtering and order books are shrinking. Not surprisingly, the jobless rate has been heading higher in each month since February, and now stands at 6½ percent, the highest level since late 1990.

European Casualties

But whereas Germany's lackluster economic performance is the result of deliberate policy design, that of such countries as the United Kingdom and France is an unwanted byproduct—a cost of rigid policy coordination which a rapidly-unifying Europe has yet to address. Lacking the flexibility to unilaterally lower interest rates in order to maintain intra-European exchange rate stability, these countries have been stymied in their efforts to jump-start their economies. Take, for example, the United Kingdom. Beset with many of the same obstacles to growth as exist in the United States—lofty debt levels, a glut of commercial real estate and slumping home prices—the U.K. recession rolls on. The economy has contracted in six of the past seven quarters, confidence has tumbled and the jobless rate, at 9.6 percent, is at its highest level in nearly five years. Yet, even though inflation has slowed decidedly, sliced from nine percent when measured on a year-over-year basis in early 1991 to less than four percent now, and wage settlements have tapered as well, the economy still suffers under

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the burden of some of the loftiest interest rates in Europe.

The policy conundrum in France is similar although, by some yardsticks, less acute. The French economy has been posting modest gains and corporate profitability has been improving, but these advances have been insufficient to prevent the jobless rate from rising almost nonstop over the past two years to ten percent of the workforce. What is more, it is by no means a sure bet that France will be able to keep its growth rate in the plus column. Business sentiment is sour, domestic spending is sluggish and export prospects are darkening—both within Europe due to faltering business activity and outside Europe by the appreciation of the franc which has accompanied the ascent of European interest rates. And, while inflation has slowed to just three percent, this has only served to push the "real" cost of borrowing ever higher, well above the tolerance levels of countless small- and medium-sized businesses which create the bulk of new job opportunities.

Recovery Complication

Realizing the far-reaching effects of their actions, the German monetary policy hawks apparently blinked in their rate deliberations,

Short Term Paper Outstanding

(Millions of Dollars)

Time Deposits $100,000 or more Weekly Reporting Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/8/92)	141,461	+ 2,923	- 47,797
New York City (7/15/92)	27,093	- 571	- 4,807
Commercial Paper (7/15/92)	542,573	- 6,955	+ 3,426

Bank Loans

(Millions of Dollars)

Commercial and Industrial Loans

Weekly Reporting Large Commercial Banks	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/8/92)	278,996	- 3,368	- 27,493
New York City (7/15/92)	48,555	+ 335	- 6,412

Total Loans and Leases Gross Adjusted

	Latest Week	Change Since Week Ago	Change Since Year Ago
Nationwide (7/8/92)	994,396	- 11,056	- 37,689
New York City (7/15/92)	160,391	- 593	- 10,869

Financial Markets

	Friday 7/24/92	Change Since Week Ago	Change Since Year Ago
U.S. Governments, Closing Yields:			
90-Day Bills†	3.22%	- .01	- 2.50
180-Day Bills†	3.32	+ .01	- 2.61
Longest Bills†	3.55	+ .08	- 2.67
Recent Issues:			
5s 6/30/94	4.21	- .03	
6⅛s 6/30/97	5.63	- .16	
7½s 5/15/02	6.73	- .16	
8s 11/15/21	7.56	- .12	
Municipals:			
Bond Buyer—20 Bond Index* (7/23/92)	6.05%	- .11	- .95
Blue List Total ($ Million)	$ 880	- $ 154	- $ 334
30-Day Visible Supply ($ Million)	$4,746	+ $1,407	+$2,660
Total	$5,626	+ $1,253	+$2,326
Corporates:			
Moody's Aa Composite (7/23/92)	8.31%	- .06	- .88
30-Day Visible Supply ($ Million)	$1,480	- $1,145	+$1,155
Stocks:			
Dow-Jones Averages:			
Industrials	3,285.71	- 45.93	+313.21
Transportation	1,273.19	- 29.70	+ 68.68
Utilities	218.52	- 15.60	+ 15.55
65 Stocks	1,153.53	- 18.16	+ 91.64
N.Y.S.E. Composite Index	226.48	- 2.03	+ 17.70
N.Y.S.E. Avg. Daily Vol. for Week (000's)	174,601	- 22,033	+26,472

*34% Taxable equivalent 9.17%.

† Bond equivalent.

International Rates

EURODOLLAR DEPOSIT RATES (bid)	Friday 7/24/92	Week Ago
Overnight	3.31%	3.38%
1 month	3.38	3.38
3 month	3.44	3.44
6 month	3.63	3.56
1 year	3.81	3.81

FOREIGN EXCHANGE SPOT RATES

New York Opening (7/24/92)	Currency Per U.S. $	Week Ago
Belgium	30.59	30.31
Canada	1.1910	1.1903
France	5.0201	4.9701
Germany	1.4860	1.4720
Italy	1127.77	1117.52
Japan	127.20	124.95
Mexico	3117.00	3115.00
Netherlands	1.6170	1.6083
South Korea	789.40	787.10
Switzerland	1.3145	1.2980
Taiwan	24.61	24.81
U.K.*	1.9153	1.9417

*U.S. $ per U.K. pound

CHEM TRADE-WEIGHTED DOLLAR (7/24/92) (Adjusted for Inflation)	Change Since Week Ago	Change Since 2/27/85
	+0.7%	-18.4%

refusing to risk the substantial progress made to date in cementing European unity. But if the straitjacket of follow-the-German-leader monetary policy pinches the hardest in Europe, it would be a mistake to think that the United States is untouched. One of the major supports of this economy has been a rising tide of export sales; two-thirds of gross domestic product growth over the past year is attributable to the U.S. exporting community. Slow growth in Europe jeopardizes this prop, and the negative consequences are already being felt.

Exports to the European Community rose by only 5.2 percent in 1991 compared with year-earlier levels, far slower than the torrid double-digit annual rates of rise experienced during the 1987-1990 period. During the first five months of this year, export growth to Europe slowed even further, rising by just 1.1 percent compared with the same period of 1991. Although rising sales to Latin America and East Asia have offset some of the slack (Financial Digest—May 4, 1992), and the recently cheapened dollar may enhance the export outlook, the actions of the Bundesbank and the resulting policy paralysis in the rest of Europe have certainly done one thing here: They have complicated the job of keeping the U.S. recovery on track.

Selected Federal Reserve Data

(Averages of Daily Figures—Billions of Dollars)

	Week Ending 7/22/92	$ Change Since Week Ago	$ Change Since Year Ago
Reserve Bank Credit			
U.S. Gov'ts and Agencies Owned Outright & RPs	281.957	+ 1.203	+24.937
Loans to Depository Inst.	.217	+ .004	- .272
Float	.294	- .138	- .055
Total Reserve Bank Credit	313.819	+ .997	+21.277
Treasury Deposits with Federal Reserve Banks	5.231	- .013	- .802
Currency in Circulation	313.942	- .531	+21.047
Gov'ts held for Foreign Acct. by F.R. Banks (End-of-Week)	288.655	+ 4.031	+45.528
Member Bank Reserves:	**7/22/92**		
Total Reserves Held	49.802	+ .152	- .630
Excess (Deficiency)	1.061	+ .022	+ .120
Net Free Reserves	.846	+ .261	+ .370
Monetary Aggregates †		**‡ % Change Since 3 Months Ago***	**Year Ago**
M1 (7/13/92)	956.5	+ 6.3	+ 11.0
M2 (7/13/92)	3,453.4	- 1.7	+ 1.2
M3 (7/13/92)	4,155.6	- 3.1	- 0.3
Domestic Nonfinancial Debt (1st Q'92)	11,304.3	+ 3.9	+ 4.5

† Seasonally adjusted.

* Seasonally adjusted annual rate.
‡ Four-week moving average.

New York Money Market

Offering Rates 7/24/92	3 Months	6 Months	1 Year
‡ U.S. Treasury Bills	3.16%	3.24%	3.41%
* Federal Agencies	3.33	3.40	3.53
* Municipal Notes–High Grade (34% Taxable Equivalent)	3.94	4.09	4.24
Negotiable Time CDs			
Chemical	Rates By Arrangement		
* Secondary Market–Prime	3.38	3.48	3.78

‡ Finance Company Paper–Prime

5- 14 days	3.18%
15- 29 days	3.28
30- 59 days	3.28
60- 89 days	3.28
90-179 days	3.28
180-239 days	3.38
240-270 days	3.40

‡* Bankers' Acceptances

Aug.	3.26%
Sep.	3.26
Oct.	3.26
Nov.	3.28
Dec.	3.30
Jan.	3.37

‡ Industrial Paper–Prime

30- 89 days	3.32%
90-120 days	3.35

†Federal Funds Effective Rate 2.88%

‡ Discount basis. *Subject to availability. † Estimated.

Selected Business Indicators

(All Dollar Figures in Billions)

	Latest Period or End of Period		Previous Period	Year Ago Period
Gross Domestic Product (Current Dollars)*	1st Q'92	$ 5,821	$ 5,740	$ 5,589
Gross Domestic Product (1987 Dollars)*	1st Q'92	$ 4,901	$ 4,868	$ 4,824
Percent Change, Annual Rate	1st Q'92	2.7	0.4	- 2.5
Change in Consumer Prices*	Jun '92n	3.6%	1.2%	3.6%
Change in CHEM Cost of Living Index*	Jun '92n	1.2%	1.2%	3.6%
Change in Producer Prices*	Jun '92	2.4%	4.8%	- 2.4%
Civilian Employment (Thousands of Persons) †	Jun '92	117,574	117,656	116,909
Unemployment as % of Civilian Labor Force †	Jun '92	7.8%	7.5%	6.9%
Personal Income*	May '92	$ 5,008	$ 4,994	$ 4,826
Leading Indicators Composite Index (1967=100) †	May '92	149.9	149.0	143.0
Industrial Production Index (1977=100) †	Jun '92n	108.2	108.6r	107.3
Net Change in Consumer Installment Credit †	May '92	- $ 2.41	- $ 3.58	- $ 1.50
U.S. Merchandise Trade Balance †	May '92n	- $ 7.38	- $ 7.06r	- $ 4.79
Plant and Equipment Expenditures*	3rd Q'92	$ 557.5(a)	$ 558.5(a)	$ 527.9
Private Housing Starts (Thousands of Units)*	Jun '92n	1,167	1,205r	1,036
New Construction Expenditures*	May '92	$ 423.2	$ 422.4	$ 399.0
Total Business Inventories †	May '92n	$ 829.1	$ 828.6r	$ 824.2r
Total Business Sales †	May '92n	$ 546.0	$ 547.1r	$ 535.4r

*Seasonally adjusted annual rate. † Seasonally adjusted. n-Newly reported figure. r-Revised. a-Anticipated.

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